price discrimination,[15] Viacom submits that, to commence an adjudicatory proceeding, a complainant should be expected to satisfy each of the following criteria:

1. it does or will actually compete for the sale of programming to consumers with a cable system holding an attributable interest in the challenged program service;[16]
2. as a result of the variance in terms and conditions, it can identify specific subscribers that it has lost to another distributor of the challenged vertically integrated program service, which distributor receives more favorable terms and conditions for such programming;
3. it will be significantly hindered or prevented from providing multichannel video program service to consumers if it cannot obtain the challenged program service on terms that are not discriminatory; and
4. the license fee paid by or offered to the complainant exceeds the license fee paid by a competing distributor

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[15] Viacom believes that different standards should be used for different types of claims. In these comments, it offers a standard to be used only in claims of price discrimination. See Part VII, infra, for a generalized discussion of standards and discovery.

[16] This requirement assumes that the programmer is subject to anti-discrimination regulation only within markets which include a commonly-owned cable system and other distributor (i.e., if the Commission adopts the proposals set forth in Part III, supra).

to whom the complainant has lost sales by more than 30%.[17]

If the complainant is not able to satisfy each of the above-listed requirements, the Commission should decline to review the matter further and should simply advise the protesting party of the standards it must meet to present a complaint that is eligible for consideration. If, and only if, all of the conditions noted above are met, would the complaint warrant such consideration.[18]

Of course, the mere fact that the price offered is outside the "zone of reasonableness" does not necessarily mean that it is discriminatory. In reviewing a complaint that satisfied the procedural requirements set forth above, the agency could determine that price differentials were reasonable and non-discriminatory for any number of reasons. For example, imposition of a price differential outside of such "zone of

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[17] The question of access to information sufficient to make this showing is discussed in Part VII, infra. This 30% is separate from uniformly offered volume discounts which the statute permits on an unrestricted basis.

[18] To the extent that the frame of reference is the rate charged by a programmer to a cable system with which it is vertically integrated, the Commission might be concerned that the price charged by the programmer is unreasonably high as a mere internal accounting transaction. To prevent that, Viacom proposes that the programmers making rates paid by their own cable systems the sole frame of reference for comparisons must certify that the rate it charges to such systems is comparable to that paid by similarly sized distributors (e.g., no more than a specified percentage above the average charge for such distributors).

reasonableness" should not be viewed as discriminatory if the defendant can demonstrate that a non-vertically integrated operator engages in similar practices.

Viacom believes that the procedures suggested herein will substantially decrease the agency's regulatory burden without in any way compromising Congress' goal of deterring anti-competitive pricing differentials arising from vertical integration.

VII. The Commission Should Ensure that the Complaint Process is Not Used By Complainants as a Means of Gaining Access to Proprietary Information

In seeking comment on the standards to be employed to determine whether a complainant has established its *prima facie* case, the Commission has asked whether the information necessary to establish such a case is readily available. *Id*.

Obviously, the information necessary to establish a case depends, in large part, on the standards required to be met. The required information must be reasonably available in order for the complaint process to have any validity. On the other hand, much of the information relating to pricing is highly sensitive and proprietary. Thus, in fashioning a standard, the Commission should avoid allowing non-*bona fide* complainants from using the process to obtain proprietary information -- or, worse, requiring parties routinely to make available proprietary information for potential complainants to review. Accordingly, the most appropriate standard is one which can be met using information already available in the public domain, but, at the same time, will deter non-bona fide complaints. If the information required is proprietary, the Commission should allow the respondent programmer to require only in camera inspection by the Commission of competitively sensitive material.

For example, under the standard set forth by Viacom in Part VI to establish a prima facie case of discriminatory pricing, Viacom submits that the following procedure should be followed. First, the complainant must have sought to resolve its dispute with the vertically integrated cable operator or programmer in good faith prior to submitting a complaint to the Commission.[19] Then, if the complainant satisfies the first three prongs of the test, the defendant would submit exculpatory rate information to the Commission for in camera inspection, together with a certification of the bona fides of the rate charged to its own local cable system.[20] Under such a procedure, the Commission could determine whether a prime facie case has been made without requiring the disclosure of proprietary rate information.[21]

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[19] That approach is similar to that used in cases involving fairness doctrine complaints, where the complainants first recourse is to the broadcaster rather than the Commission.

[20] See supra, 18.

[21] As an alternative, the defendant should have the option to submit the material to an independent arbitrator for in camera inspection to allow the arbitrator to make the determination.

Once a prima facie case has been made, the Commission asks what level and forms of discovery should be permitted. NPRM at ¶ 45-47. With regard to claims of price discrimination, Viacom submits that no discovery should be allowed. Once the prima facie case is made, the burden of producing evidence would shift to the program distributor. In meeting this burden and as an affirmative defense sufficient for the Commission to summarily dismiss a claim without further investigation, the program distributor would be permitted to place into evidence the fact that the difference in the license fee in excess of 30% paid by a competing distributor of the complainant is attributable to uniformly offered volume discounts to which the competing distributor is legitimately entitled. If the affirmation defense has not disposed of the issue, then the program distributor would determine what to produce in order to demonstrate the legitimacy of any price differential.

In responding to discovery requests in general, Viacom submits that parties should be permitted to redact proprietary information not relevant to the resolution of the complaint. See id at ¶ 47. Viacom also supports the use of a protective order strictly limiting examination of the documents produced and the imposition of severe sanctions on those who fail to abide by the terms of the protective order.[22] Similarly, the penalties

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[22] Indeed, given the proprietary nature of the information, Viacom believes that, at the request of the (continued...)

imposed for the filing of frivolous complaints should be such that they deter the filing of non-bona fide complaints. See NPRM at ¶53.

VIII. Buying Groups Should Be Required to Agree to Unitary Treatment Before Being Eligible for Volume Discounts

The Commission also seeks comment "on issues relevant to defining the class of 'agents' or 'buying groups'" covered by Section 628(c)(2)(B). NPRM at ¶26. Viacom believes that, as the Commission suggests, the Commission should require "buying groups" seeking the benefits of price discounts based on size "to agree to unitary treatment for other relevant purposes." Buying groups seeking such price discounts should be subject, at a minimum, to joint billing, uniform contract provisions, and joint and several liability under a single affiliation agreement. Joint and several liability should pertain at least to the guaranty of payment of license fees to the programmer if not to other types of general liability such as for copyright infringement. Thus, if a buying group actually performed the same functions and offered the same benefits to programmers as an MSO, it would be entitled to comparable treatment. Viacom believes that this interpretation is just and fair. To interpret

[22](...continued)
respondent, the Commission's staff should review the material to determine whether it is sufficient to refute the claim. If so, the complaint should be dismissed.

the statute in a contrary manner would be inequitable because it would allow the members of a buying group to rely on their membership status in order to attain the benefits of a lower price but would then deny such membership status for all other purposes, including the obligations that would normally arise from it.

Antitrust jurisprudence provides a helpful analogy. Although courts have been willing to permit competitors to form buying groups, they have refused to do so when the group was found to be nothing more than "a 'sham' organization seeking only to combine otherwise independent buyers in order to suppress their otherwise competitive instinct to bid up price." Kartell v. Blue Shield of Massachusetts, Inc., 749 F.2d 922, 925 (1st Cir. 1984), cert. denied, 471 U.S. 1029 (1985); see also United States v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940) (horizontal price-fixing purchasers held per se illegal); Vogel v. American Soc'y of Appraisers, 744 F.2d 598, 601 (7th Cir. 1984) ("buyer cartels, the object of which is to force the prices that suppliers charge the members of the cartel below the competition level, are illegal per se").

Courts have upheld buying groups under the antitrust laws where they have been formed for legitimate business purposes in achieving economies of scale or other efficiencies. In Northwest Wholesale Stationers Inc. v. Pacific Stationery & Printing Co., 472 U.S. 284 (1985), for example, the Supreme Court recognized that a purchasing cooperative of office supply retailers achieved economies of scale explaining:

> The arrangement permits the participating retailers to achieve economies of scale in both the purchase and warehousing of wholesale supplies, and also ensures ready access to a stock of goods that might otherwise be unavailable on short notice. The cost savings and order-filling guarantees enable smaller retailers to reduce prices and maintain their retail stock so as to compete more effectively with larger retailers.

472 U.S. at 295.

In order to ensure that the buying groups are not sham organizations formed merely so that the members of the group could obtain a lower price, it is appropriate for the Commission to look for indicia of the bona fides of the buying group, which, at a minimum, should include all of the factors noted by the Commission in paragraph 26 of the NPRM.

IX. The Commission Properly Concluded that Section 628 Should Not be Applied to Existing Contracts and Should Find There is No Need to Establish a Prospective Deadline for Compliance

The Commission tentatively has concluded that "any pricing policies or restrictions developed to implement Section 628 should not be applied retroactively against existing contracts." NPRM at ¶27. Viacom supports this conclusion and submits that the Commission need not, at this time, establish a prospective deadline for compliance.

As the Commission properly notes, the Act "is silent concerning the enforcement of the anti-discrimination rules with respect to existing contracts." Id. It is well settled that courts disfavor retroactive application of a federal statute in the absence of an express directive from Congress.

> "Congressional enactments and administrative rules will not be construed to have retroactive effect unless their language requires this result. . . . By the same principle, a statutory grant of legislative rulemaking authority will not, as a general matter, be understood to encompass the power to promulgate retroactive rules unless that power is conveyed by Congress in express terms.") (emphasis added).

See, e.g., Bowen v. Georgetown University Hospital, 488 U.S. 204, 208 (1988) (citations omitted). Thus, the absence of such a provision here cannot be read to imply Congressional intent to "require" "in express terms" preemption or modification of existing contractual arrangements.

Where Congress intended to deal with the question of retroactivity -- either by providing for only limited grandfathering of existing contracts or by authorizing their abrogation -- it specifically did so. For example, Section 628(h) states that, with one exception dealing with unserved areas, nothing in the program access provisions of the Act "shall affect any contract that grants exclusive distribution rights . . . . that was entered into on or before June 1, 1990." Thus, this limited grandfathering provision in Section 628 indicates that Congress was aware of the need specifically to apply retroactive effect to its legislation if it so desired.[23]

Even if the Act could somehow be read as allowing the Commission to apply the rules to implement Section 628 retroactively, there are serious constitutional implications to any retroactive application of the Act to existing contracts:

> Retroactive legislation presents problems of unfairness that are more serious than those posed by prospective legislation, because it can deprive citizens of legitimate expectations and upset settled transactions. For this reason, "[t]he retroactive aspects of [economic] legislation, as well as the prospective aspects, must meet the test of due process": a legitimate legislative purpose furthered by rational means.

General Motors Corp. v. Romein, ___ U.S. ___, 112 S.Ct. 1105, 1112 (1992), quoting Pension Benefit Guaranty Corp. v. R.A. Gray & Co., 467 U.S. 717, 730 (brackets in original).[24]

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[23] Similarly, Section 614(b)(10)(C), provides that a cable operator may continue to receive carriage payments from a local commercial television station until the expiration of any governing agreement entered into prior to June 26, 1990.

[24] Generally, retroactive economic legislation is upheld as a method of spreading costs among the parties who have benefitted from the activity that led to the costs being incurred, but not as a method of abrogating contractual rights bargained for in anticipation of future performance. See U.S. v. Sperry Corp., 493 U.S. 52 (1989); National Railroad Passenger Corp. v. Atchison, Topeka & Santa Fe Railway Co., 470 U.S. 451 (1985); Pension Benefit Guaranty Corp. v. R.A. Gray & Co., 467 U.S. 717 (1984); Usery v. Turner Elkhorn Mining Co., 428 U.S. 1 (1976). For a more complete discussion of the constitutional implications of retroactive application of the rules, see Comments of Viacom International Inc. in MM Docket No. 92-259 (Broadcast Signal Carriage Issues), at 13-21.

A severe upheaval would result from the abrupt renegotiation of the myriad array of existing contractual relationships between program services, on the one hand, and cable and non-cable distributors, on the other, if the anti-discrimination rules were applied retroactively to existing affiliation agreements. SNI and MTVN have entered into costly programming contracts based on the revenues they legitimately expect to receive from their existing affiliation agreements. To force the premature renegotiation of such affiliation agreements may preclude programmers from honoring their commitments to program suppliers. Among other things, this would run counter to the recognized Commission goals of promoting investment in programming and encouraging the diversification of programming services. A high degree of certainty is needed during the remaining terms of existing affiliation agreements. In order to attract capital or to justify a large expense in the acquisition of programming and the development of a program service, programmers in turn need assurance that their sources of revenue, i.e., their affiliation agreements, will continue until their respective negotiated termination dates and that the negotiated revenues under such agreements will be forthcoming throughout their terms. Moreover, because affiliation agreements often provide for higher payments by affiliates in the latter stages of the contract in exchange for lower payments in the earlier stages, renegotiation would allow such affiliates to gain something for which they have not bargained.

Viacom submits that an appropriate standard for reviewing the rationality of retroactive application of the Act to agreements for future economic benefits is the four-factor test set for in Nachman Corp. v. PBGC, 592 F.2d 947, 960 (7th Cir. 1979), aff'd on other grounds, 446 U.S. 359 (1980): (1) the reliance interests of the parties affected; (2) whether the impairment of the private interest is affected in an area previously subjected to regulatory control; (3) the equities of imposing the legislative burdens; and (4) the inclusion of statutory provisions designed to limit and moderate the impact of the burdens.[25]

These four factors weigh heavily against retroactivity. First, it is clear that in entering into long-term program production and acquisition agreements, program services have heavily relied on the revenues contemplated in existing

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[25] In Pension Benefit, supra, the Supreme Court rejected the constitutional underpinnings of the Nachman test as applied to cases where the retroactive legislation affects economic benefits and burdens, but left open the possibility that there might be other circumstances under which the four Nachman factors might be relevant. Pension Benefit at 727, n.1. Viacom submits that the due process and First Amendment implications of retroactive application of the Act to affiliation agreements at least renders the four Nachman factors relevant for the purpose of determining whether retroactive application of the Act is constitutional. Since, as set forth below, all four of the Nachman factors militate against retroactivity, the Nachman tests in combination are sufficient to show that retroactive application here would deny due process.

affiliation agreements with distributors. Both types of services -- premium and advertiser-supported -- have relied heavily upon such revenues in establishing the levels of their own commitments to meet programming and other costs.

Second, neither the rights established in existing affiliation contracts nor the rights established in existing contracts between program services and their suppliers of programming have been previously subject to any federal regulatory control.

Third, the Commission should not underestimate the potential disruption to a program service if it allows existing affiliation agreements to be abrogated. If so, the program service may be unable to meet the subscription levels which form part of the basis for its affiliation with the distributor. An advertiser-supported service will face the same or similar consequences from the loss of subscription levels and in addition will very likely be unable to meet the viewership levels it has guaranteed to advertisers, thus subjecting itself to refund and make-good obligations. As stated, program services have already agreed to pay their program suppliers in reliance on these anticipated subscription and/or viewership levels. Thus, assuming that the program service is unable to terminate or modify its existing contracts with program suppliers, abrogation of affiliation agreements will have a further significant economic effect: aside from losing revenue, the program service may be unable to pay programming fees which assume a minimum level of revenue premised on the existence of the very affiliation agreements that are being abrogated.

Fourth, there is nothing in the Act which would mitigate any abrogation of existing affiliation contracts. For instance, the Act does not specify remedies available to a program service once its affiliation contract has been abrogated. The Act also does not insulate a program service from liability in the event it cannot meet its obligations to program suppliers or to advertisers in the event of abrogation.

In sum, the Act plainly does not require that its anti-discrimination provisions be given retroactive effect. This alone prohibits retroactive application. Beyond this, given Congress' general disposition throughout the Act against overriding existing contracts, the constitutional impediments to retroactive economic legislation generally, and the very real and substantial practical problems associated with abrogation, Viacom urges the Commission to adhere to its tentative conclusion that "pricing policies or restrictions developed to implement Section 628 should not be applied retroactively against existing contracts."

The Commission also asks whether a claim of discrimination may be based "on comparisons with contracts that predate the rules, or rather, only other contracts entered into under our new rules. _NPRM_ at ¶27. Viacom recognizes that a flat ban on use of pre-existing contracts as a basis for rate comparisons would result in a situation in which a complainant might have no basis to make a showing of discrimination. Accordingly, it submits that the point of comparison for determining whether the new contract rates offered to the complainant are reasonable should be the <u>then effective</u> rate paid by a competing distributor vertically integrated with the program service, even if it is the result of an agreement executed prior to the effective date of the rules.

To the extent the geographic scope of the adjudicatory inquiry is larger than that proposed by Viacom, the comparison should be only to agreements entered into after the effective date of the new rules. Pre-existing agreements with non-vertically integrated affiliates, having been executed under widely differing circumstances, simply would not provide a valid basis for comparison. Vertically integrated video programmers would be subjected to <u>severe</u> financial hardships if new agreements were compared to the lowest prices offered to other distributors prior to promulgation of the FCC's implementing regulations.

X. The Commission Should Allow Operators to Enter Into Exclusive Distribution Agreements With New Program Services

Section 628(c)(2)(D) prohibits exclusive contracts between a cable operator and an affiliated programmer within the cable operator's service area unless the Commission determines the exclusive contract is in the public interest. 47 U.S.C. § 628(c)(2)(D). The Commission asks whether it should find that exclusive contracts with cable operators for new program services are in the public interest. NPRM at ¶36.

In determining whether a grant of exclusive rights to cable operators is in the public interest, the Commission must consider, among other things, the effect of such grant on the development of competition in programming and the attraction of capital investment in the production and distribution of new programming. Section 628(c)(4). Although SNI and MTVN are not now parties to any exclusive agreements with cable operators,[26] Viacom submits that such agreements between cable operators and new program services can be consistent with the public interest. In fact, Viacom's cable systems in the San Francisco Bay area recently helped to develop a new foreign language cable service (the Jade Channel). As an inducement to and in exchange for its involvement and carriage of the untested service, Viacom was

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[26] In a few instances, there are exclusive agreements relating to the launch of the new program service Comedy Central.

granted exclusive rights to distribute the service for a period of time. Such agreements encourage investment in and carriage of new services and will enable the cable operator to develop marketing plans to increase the viability of the new program service.[27] Thus, by allowing limited cable exclusivity for new program services, the Commission will enhance the diversity of programming. Viacom submits that a reasonable duration for exclusive cable contracts involving new program services is 10 years. This time frame will enable the new program service to establish itself while providing the cable operator with a legitimate expectation that its marketing expenses and inherent risk in carrying the new program service will be rewarded.[28]

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[27] The Commission is aware of the "free rider" phenomenon, whereby one distributor will seek to attract subscribers based on the marketing efforts of another. This has the effect of generally discouraging investment in marketing by distributors.

[28] Moreover, because Section 616 precludes cable operators from <u>requiring</u> exclusivity as a condition of carriage, Cable Act of 1992, § 616(a)(2), a programmer will only enter into an exclusive contract with a cable operator if it believes it necessary to promote the development of its new service.

XI. The Operations Of Viacom's Program Services Illustrate The Pro-Competitive Character Of Pricing Differentials Permitted Under The Act

The zone of reasonableness set forth in Section VI is the appropriate standard because Congress expressly recognized that there could be price differences both within and between cable and non-cable distributors that have nothing to do with any misuse by the vertically integrated entity of its interest in a program service in order to prevent competition to its cable systems. For example, a programmer can impose requirements -- such as higher license fees -- to take into account significant differences between the distributors in terms of "creditworthiness," "financial stability", "character" or "technical quality". See Section 628(c)(2)(B)(i). Similarly, a programmer's price disparity could reflect nothing more than "actual and reasonable differences in the cost of creation, sale, delivery or transmission" of video programming, either at the programmer's level or at the distributor's level. See Section 628(c)(2)(B)(ii); 138 Cong. Rec. S16,671 (daily ed. Oct. 5, 1992). Moreover, price differences would also be permissible under the statute if they reflected "economies of scale, cost savings, or other direct and legitimate economic benefits reasonably attributable to the number of subscribers served by the distributor." See Section 628(c)(2)(B)(iii).

The experience of SNI and MTVN confirms that Congress was correct in recognizing that programmers are justified in charging different prices to distributors who are not similarly situated. While the experiences of SNI and MTVN are generally similar, there are certain important differences between premium and advertiser-supported programmers which, where relevant, are dealt with separately below.

A. SNI's premium services: Showtime, The Movie Channel and FLIX

Showtime and The Movie Channel are widely distributed through the alternative technologies of HTVRO, SMATV and MMDS.[29] The overriding incentive behind SNI's distribution policies is to increase the size of its subscriber base over which it can amortize the cost of its programming (primarily, recently-released movies). The absolute size of that subscriber base, and its size relative to the subscriber bases of competitors bidding for the same programming rights, are both important factors. Every incremental subscriber thus presents an important opportunity to grow and to grow relative to the size of its premium competitors. SNI makes distribution decisions regarding new technologies based on its judgment as to whether a proposed affiliation arrangement will lead to incremental subscriber growth. Currently, the ancillary markets (SMATV, MMDS (including MDS), HTVRO and SMATV to hotel/motel and hospitals) account for over 12% of SNI's premium subscriber base. As detailed below,

[29] FLIX was launched in August 1992 and currently enjoys only limited distribution.

where price disparities exist in the license fees paid by cable operators and those paid by alternative distribution technologies, there are valid and substantial reasons for such differences.

B. MTVN's services: MTV, VH-1 and Nickelodeon

Because MTVN's services are largely advertiser-supported, MTVN has always sought the broadest possible distribution for its services. Advertising revenue comprises approximately 65% of MTV's and Nickelodeon's total revenue and 95% of VH-1's total revenue. (License fees paid by affiliates comprise most of the remainder.) MTVN's services are made available to all SMATV and MMDS operators who request them, and are nationally available in the HTVRO market through SSN's and others' program packages.[30]

[30] Because of the access to the national HTVRO retail market afforded by SSN (Viacom's owned and operated satellite distribution service to the HTVRO market), MTVN and SNI have been more selective with respect to licensing their programming to other national HTVRO retailers. In this connection, the Commission has asked for comment (NPRM ¶ 13) as to whether certain "practices that are precluded by the antitrust laws -- such as refusals to deal or tying arrangements -- are encompassed within the terms of Section 628 and warrant Commission regulation." Viacom opposes such a broad application of Section 628(c). There plainly is no factual record to support such an interpretation and no indication that the antitrust laws are not adequate to address such issues if and when they arise.

C. Volume discounts reflect a "legitimate economic benefits" to SNI and MTVN

SNI's and MTVN's license fees are not uniform for each distribution technology. Rather, there is a range of rates that are a function of various factors. For SNI's premium services, these include, the ratio of Showtime and The Movie Channel subscribers to basic subscribers, the retail rate charged by the affiliate, and whether a subscriber purchases one or more premium services (multipay discounts), marketing commitments and a number of other variables. SNI's application of these factors is intended to create incentives for distributors to price Showtime and The Movie Channel attractively to consumers and sell as many subscriptions as possible. Congress has recognized that such price differences are permissible where, as here, they result from the programmer enjoying economies of scale, cost savings or other direct and "legitimate economic benefits reasonably attributable to the number of subscribers served by the distributor" (see Section 628(c)(2)(B)(iii)).

Most importantly, because cable operators historically have been able to deliver a vastly greater number of customers than any other type of distributor, they generally have paid lower programming license fees. Cable's greater subscriber potential accounts for most of the disparity between rates negotiated with cable operators and rates negotiated with non-cable distributors. Most cable systems are owned by MSOs that deliver a volume of customers that far exceeds the customer base of even the largest non-cable distributors. For premium services, these MSOs also generally either contractually commit to promote and sell Showtime and The Movie Channel (or have established track records of doing so), which, together with license fees paid, constitutes important consideration (i.e., the statute's "legitimate economic benefit") to SNI. Thus, comparing the license fees charged to cable operators as a whole with those charged to alternative distributors as a whole, which cannot benefit SNI with either a large subscriber base or similar promotional commitments, is to compare apples to oranges.

Because MTVN's program services rely so heavily on advertising revenues, which are directly related to the number of actual and potential viewers of a program or programming service, MTVN generally negotiates more favorable license fee rates with distributors that can deliver the broadest distribution. MTVN negotiates higher license fees with non-cable distributors because they do not have the ability to deliver MTVN's services to a large group of subscribers and, therefore, do not provide the basis for meaningful or material additional advertising revenue.

There can be no doubt that MTVN receives real economic benefit in the form of incremental increased advertising revenue when it adds a sufficiently large number of subscribers (as distinguished from small, incremental numbers of subscribers) so that it merits an increase in its advertising rates. Thus, MTVN legitimately seeks to reward those distributors providing sufficiently large subscriber growth necessary for MTVN to receive greater advertising revenues.

Television advertising rates are a function of the size of the television audience reached by a program service (reach) and the percentage of that audience watching the service at any given moment (rating). MTV and Nick currently reach approximately 50 million homes each and average a .5 rating. VH-1 reaches approximately 40 million homes and averages a .2 rating. With their current reach and ratings, MTV and Nick would each need to grow by 10 million subscribers to demand higher advertising rates. VH-1 would need to grow by 20 million subscribers to raise its advertising rates. The entire universe of television households currently accessible through non-cable distributors is significantly less than the number of television households currently accessible via cable and does not provide for sufficient additional distribution necessary to achieve meaningful additional advertising revenues. Therefore, there is no economic incentive for MTVN to negotiate lower license fees for the distribution of its services by these smaller non-cable distributors.[31]

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[31] To illustrate, each individual non-cable distributor typically provides only a few thousand subscribers. The addition of these subscribers has virtually no impact on MTVN's revenue because they are too (continued...)

Cable operators are subject to additional charges if they offer MTVN's services on a tier of services for which the cable operator imposes an additional charge on its subscribers, because the tiering of MTVN's services tends to reduce the number of subscribers and viewers. Tiering surcharges thus compensate MTVN for the anticipated loss in advertising revenue, confirming that advertising revenue implications drive MTVN's license fees decisions.

D. SNI and MTVN incur higher administrative and transactional costs when serving non-cable markets

Although Section 628 prohibits "discrimination" in prices, terms and conditions of sale, Congress made clear that a programmer is not prohibited from "establishing different prices, terms, and conditions to take into account actual and reasonable differences in the cost of creation, sale, delivery or transmission of satellite cable programming." Sec. 628(c)(2)(B)(ii). Similarly, Congress also expressly provided that a programmer is not prohibited from establishing price differences "which take into account economies of scale, cost savings, or other direct and legitimate economic benefits reasonably attributable to the number of subscribers served by

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[31](...continued) inconsequential to affect advertising rates. By contrast, the top 10 cable affiliates have an immediate and direct impact on advertising revenue.

the distributor". Sec. 628(c)(2)(B)(iii). Under this subsection, a price difference is permissible even if it is not cost justified; such a justification is required only for purposes of subsection 2(B)(ii). A volume discount that provides SNI "legitimate economic benefits" by inducing distributors to increase the penetration of SNI's programming services is permissible even in the absence of a cost justification. In licensing its programming services to distributors, SNI and MTVN have experienced differences in cost that Congress expressly found to be a valid basis for charging different prices to different distributors.

For example, SMATV, MMDS and HTVRO distributors provide a much smaller subscriber base than cable operators typically do. As a result, the administrative and transaction costs associated with the delivery of service to each non-cable subscriber are greater than they are where delivery is to a cable subscriber. To illustrate the point, each of SNI's top 10 cable affiliates alone generates more subscribers than the total number of SNI's residential MMDS and SMATV subscribers. To reach these residential SMATV and MMDS subscribers, SNI has negotiated agreements with 164 affiliates. Indeed, SNI's top 40 MSO affiliates yield 90% of SNI's cable subscribers. The same pattern holds true for MTVN. Yet, every affiliate transaction, regardless of the distribution technology, incurs similar administrative costs, such as negotiating an agreement,